The American Consumer Institute
Center for Citizen Research

14 December 2020

To: OECD Centre for Tax Policy and Administration

Comments by the American Consumer Institute Regarding the Public Consultation Document for the Reports on the Pillar One and Pillar Two Blueprints (Sent via email to cfa@oecd.org)

Dear Sir or Madam:

These comments are submitted on behalf of the American Consumer Institute (ACI), a 501(c)(3) nonprofit, non-partisan, educational, and public policy research organization with the mission to identify, analyze, and project interests of consumers in selected legislative and rulemaking proceedings in matters that affect consumers. ACI appreciates the opportunity to submit these comments on the OECD/G20 Base Erosion and Profit Shifting Project, specifically on the *Tax Challenges Arising from Digitalisation – Reports on the Pillar One* and *Pillar Two Blueprints*.

1. Not Seeing the Forest for the Trees

Pillar One is designed to address the explosive growth of the digital economy that has been supposedly eroding the OECD's tax base. The Blueprint plan would construct a legal framework for profit shifting that would permit some countries to have taxing authority over the corporate income conventionally booked in countries where corporate operations are physically present.

Pillar Two proposes to set a global minimum tax rate on large multinational companies in the hopes of reining in tax arbitrage and stopping companies from venue shopping. Our comments to follow will show that both Pillar One and Pillar Two would impose significant and discriminatory costs that would adversely and unfairly impact certain countries, industries, services, and ultimately consumers.

In soliciting comments on the two reports, the OECD asks a number of specific and detailed-oriented questions dealing with various technical aspects of the Blueprint, including issues involving thresholds, processes, factors, model rules, and administrative burdens and other complexities. However, looking at the totality of the Pillar One and Two plans, we conclude that the international community should pause and comprehensively reevaluate approach, because commenting on the minutia of the Blueprint would be tantamount to accepting a number of serious overarching flaws. We ask that the OECD to take a step back and reconsider this Blueprint.

Our comments contained herein will discuss these major flaws: implementing inconsistent and discriminatory tax rules; undermining competition; establishing an international tax cartel; utilizing a risky value-creation principle; contributing to damage to the environment, the world economy, and long-term technological innovation; and implementing tax changes that disproportionately impact poorer and low-tax nations.

We believe that commenting on the minutia of the Blueprint proposal will, at this time, only serve to make marginal improvements to an inferior tax plan. In order to achieve an optimal and fair plan, we conclude that addressing these fundamental flaws should be the first step in finding a final workable plan that best serves the OECD's member countries and their respective citizens. Ironing out the specific details should come later.

2. The Lack of a Theoretical Foundation Shows Subjectivity, Not Objectivity

During the OECD presentation on October 12th, Secretary General Angel Gurria explained that large tech firms would be a "good source" of tax revenue because big tech was not as hurt by the COVID pandemic as other businesses were.[1] This statement by the Secretary General is quite disturbing, because it suggests the tax plan is more concerned with raising tax revenues than it is about finding an equitable international tax model.[2]

Motivations aside, the Blueprint is full of inconsistencies where different tax rules are applied across different services, industries, firm sizes, and national borders. For example, the tax plan generally singles out large firms (those greater than 750 million Euros) and, in particular, singles out a few large U.S. online technology firms for taxation, as well proposing rules that would adversely affect low-tax nations and lesser developed nations. As will be discussed later in these comments, the Blueprint proposes a wide range of carveouts that protect some firms but not their direct competitors. Consistency and objectivity should matter.

The tax discrimination provisions in the Blueprint are not supported by widely accepted financial and economic principles. We believe that these inconsistencies create inequities that could have disastrous international tax and trade implications. For the tax plan to be successful,

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[1] "International Taxation: Addressing the Tax Challenges Arising from Digitalisation of the Economy," OECD WEB TV, Oct. 12, 2020, https://oecdtv.webtv-solution.com/7020/or/international_taxation_addressing_the_tax_challenges_arising_from_digitalisation_of_the_economy.html.

[2] Portions of these comments to follow are taken directly from Steve Pociask, The OECD's Big Tech Cash Grab, *Real Clear Policy*, https://www.realclearpolicy.com/articles/2020/11/04/the_oecds_big_tech_cash_grab_582914.html, November 4, 2020.

it must be totally objective and not discriminatory. Therefore, we strongly recommend the OECD take pause and reconsider its approach at this time.

3. The Loss of National Sovereignty

The proposed Pillar One and Pillar Two rules would effectively transfer taxing rights between countries, including allocating shares of taxable profits, determining which country should have tax authority, and setting a minimum tax rate. In this regard, the Blueprint is a major undertaking, and it will impact the taxing authority of individual countries in significant ways, including changing jurisdictional nexuses and eroding national sovereignty.

Taxes on businesses do not spare consumers the costs. Like tariffs, if taxes increase, consumers will ultimately pay higher prices for goods and services. While taxes are necessary to provide vital public services, when taken too far, excessive taxation can be an impingement on the basic freedoms and liberties of a nation's citizens, as well as negatively impact economic growth and the standard of living of citizens. The world's tax base should not be used to fund or prop up high-tax nations, authoritarian governments, and socialist programs at the expense of more fiscally responsible and representative governments.

In democracies across the globe, citizens should have the right to elect or "vote out of office" government representatives and political candidates based on their policy positions, including their tax policies. However, minimum tax rates, as proposed in Pillar Two, usurp the authority of sovereign nations. The OECD plan would allow "taxation without representation."[3]

Simply putting world's tax base on the table for others to share undermines the need for public accountability and it infringes on basic human rights and freedoms. It is not the role of the OECD to fund big government. Put succinctly: taxing should be a matter between self-governing nations and their citizens, and not a power to be relinquished to an international body having absolutely no accountability to the citizens of the world.

4. Pillars One and Two Would Unquestionably Harm the Environment

Regarding Pillar Two, when it comes to global warming, there is great irony to the Blueprint's consequences on the environment, sustainability, and mitigating climate change.[4] While President-elect Biden promised to rejoin the Paris Agreement, under the proposed Blueprint, taxes will now be applied to such international services as insurance and reinsurance – the very services needed to backstop against storms, protect citizens from catastrophic

[3] "Taxation without representation is tyranny," is the full slogan by the thirteen American colonies and was used to describe taxation under British rule, see https://www.investopedia.com/terms/t/tax_without_representation.asp.
[4] Excerpt taken from Steve Pociask, "OECD Tax Plan: Joe, Just Say No," *Morning Consult*, https://morningconsult.com/opinions/oecd-tax-plan-joe-just-say-no/.

events like earthquakes, and incentivize mitigation and resilience. While the OECD claims to be concerned about global warming and investing in sustainable infrastructure, Pillar Two would tax the world's means for protecting itself against the harmful effects of climate change.[5] These taxes would undeniably lead to significantly higher insurance premiums for consumers, businesses, and governments, thereby discouraging their use and creating moral hazard.

Regarding Pillar One, many empirical studies have demonstrated that broadband and information technology services reduce and avoid energy use, and thus help the environment. This is evident in how these technologies affect where we work, how we shop, and what we consume. For instance, electronic communications and messaging services have reduced the demand for first-class letters and newspaper subscriptions, which, in turn, have reduced the need for paper, saved trees, conserved energy, reduced water pollution, and decreased greenhouse gas emissions into the atmosphere.

As employees work from home, billions of gallons of gasoline are saved in the U.S. each year. While e-commerce also means fewer cars are driven on the road, it also means that less square footage of commercial, retail and wholesale facilities are needed, which saves the energy required to build and operate these facilities. As workers teleconference, business travel is reduced, which spares the emission of greenhouse gases. While there are countless such examples, it is clear that internet applications affect how people shop, communicate, travel, work, and use digital products that are environmentally friendly. If improving the environment is a key topic of serious concern, as the OECD suggests, its tax policy should be in harmony with these concerns.[6]

One study estimated online technology applications to have reduced U.S. greenhouse gas emissions by more than 1 billion tons over a ten-year period – including savings related to business-to-business and business-to-consumer e-commerce (206 million U.S. tons), telecommuting (560 million tons), teleconferencing (200 million tons), and the reduction in paper and plastics (125 million tons).[7] Lawrence Berkeley National Lab found that, for a 10-year period, the tech economy could decrease the growth of carbon emissions by 67% over what would otherwise occur.[8] In addition to the fuel savings from telecommuting, Romm estimated that home offices use significantly less energy than a commercial office and would avoid the construction of office space, thereby reducing greenhouse gas emissions.[9]

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[5] For an example of the OECD's concerns on environmental issues, see http://www.oecd.org/env/cc/; and in support of investing in sustainable infrastructure, see https://www.oecd.org/finance/sustainable-infrastructure.htm.

[6] For more, see the OECD's webpages on the environment at http://www.oecd.org/environment/.

[7] Joseph P. Fuhr, Jr. and Stephen B. Pociask, "Broadband Services: Economic and Environmental Benefits, American Consumer Institute, October 31, 2007.

[8] Robert D. Atkinson and Andrew S. McKay, "Digital Propensity: Understanding the Economic Benefits of the Information Technology Revolution," The Information & Technology Foundation, Washington D.C. March 2007, p. 27.

[9] Joseph Romm, "The Internet and the New Energy Economy," Center for Energy and Climate Solutions, Global Environment and Technology Foundation, 2002.

To summarize, both Pillars One and Two will lead to higher tax collections, and therefore increase costs on insurance and reinsurance, impede infrastructure resilience and mitigation, and delay innovations that would reduce pollution and emissions for years to come. At this crucial time and in the face of global warming, the OECD is proposing taxation of the very services that so clearly benefit the environment.

5. The Value-Creation Principle is Inappropriate

The OECD's article 5 Model Tax Convention on Income and Capital specifies that when a business has no permanent address in a particular country then it is not subject to that country's taxes. On the other hand, the Pillar One Blueprint rejects this international convention and uses a value-creation methodology as a determinant for taxing digital services. More specifically, Pillar One imposes the following rule: if a digital product or service is consumed and enjoyed in Country A, but was created and managed by a large company with an established residency in Country B, the company is now taxable by Country A. This rule measures the degree that consumers use digital services based on "where economic activities take place and value is created."[10]

According to this logic, if a consumer in Germany "likes" a picture while using a free social media application, the high-tech firm has created value for the German consumer, and this activity would now be taxable. This principle applies to primarily large U.S. high-tech services and not other goods and services.

The value-creation principle uses convoluted logic. Economics teaches us that consumers always experience "value" whenever they consume a "normal" good or service, not just high-tech services. So, if I buy and consume Danish cheese and Argentinian Wine in my home in the U.S., under a value-creation methodology, shouldn't these foreign manufacturers also pay U.S. taxes for creating value for me in the U.S.? By only applying these taxing principles to the high-tech sector, the Blueprint makes it clear that the purpose of this proposal is to target primarily U.S. high-tech firms. In this way, the use of a value-creation principle is illogical, protectionism, inconsistent, unfair, grossly discriminatory, and inappropriate.

Because Pillar One exposes these businesses to taxation in countries where they have no permanent presence, the Blueprint turns international norms on its heads, which could pose a global risk in the future. One day, for example, China could develop a new tax system on foreign products sold in China as a means to target imports and to protect is own domestic economy. In addition, if the value-creation principle were indiscriminately applied across all industries, countries with trade deficits, including the U.S., would want to expand this user-

[10] "Guidance for Tax Administrations on the Application of the Approach to Hard-to-Value Intangibles -- Inclusive Framework on BEPS: Action 8," OECD, June 2018, guidance-for-tax-administrations-on-the-application-of-the-approach-to-hard-to-value-intangibles-BEPS-action-8.pdf (oecd.org).

based scheme to include its imports and consequently expose more of the world's tax base. We conclude that the adoption of this user-based scheme is risky and, in the future, would create a very slippery slope. This value-creation principle should be soundly rejected.

6. The OECD Should Protect Competition, Not Collusion

Pillar Two proposes establishing a minimum wage that would dissuade corporations from venue-shopping. But is venue shopping really a bad thing? The reality is that taxes can be an effective means for nations to compete, just like some countries attract businesses by offering lower wages, subsidies, and other incentives. By setting a minimum tax rate, Pillar Two's plan is tantamount to a price fixing scheme. The U.S. Federal Trade Commission defines price fixing as an agreement among competitors to "raise, lower, or stabilize prices" and effectively reduce competition.[11] In this case, raising taxes in low-tax countries would raise business prices and undermine these countries ability to compete against larger and more developed nations. This is especially the case for underdeveloped and poorer nations that rely on taxes as a means to incentivize investments. The development of an international tax cartel would severely harm countries, businesses, and consumers.

In fact, venue shopping is good for competition and consumers. For example, imagine you are going to buy a pair of shoes from a store for $100, but the store says it will cost $140 after adding hefty convenience fees.[12] When you check the shoe store across the street, you find that the same $100 pair of shoes for only $105 after the fees. Comparison shopping saves consumers money; it rewards market winners; it disciplines price gougers; and it increases social welfare. In this way, venue shopping is good for consumers.

However, what if all shoe stores were required to set the same level of surcharges? That is exactly what the OECD's Pillar Two proposal proposes to do by setting a minimum tax. It discourages competition between countries. This coordination is no different than price fixing. It undermines the ability of nations to attract capital investment, lure manufacturing back into its borders, and retain and protect a country's tax base. This also means that imposing a minimum tax will lead to increased tax base erosion in low-cost nations and in poorer nations – exactly what the Blueprint should want to prevent.

The point is that coordinating fees is anticompetitive and anti-consumer. If businesses were colluding, it would certainly be regarded as an antitrust violation. Price fixing is bad for consumers and the global economy.

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[11] See the U.S. Federal Trade Commission website for their definition at https://www.ftc.gov/tips-advice/competition-guidance/guide-antitrust-laws/dealings-competitors/price-fixing.

[12] This example is from Steve Pociask, The OECD's Big Tech Cash Grab, *Real Clear Policy*, https://www.realclearpolicy.com/articles/2020/11/04/the_oecds_big_tech_cash_grab_582914.html, November 4, 2020.

To summarize, given that some governments own, subsidize, and incentivize their domestic commerce, and that average wages and purchasing power varies between nations, a minimum tax will hamper the ability of countries to overcome these discrepancies, attract commerce and compete. The Pillar Two tax proposal appears to be focused on raising tax revenue, creating an international tax cartel, protecting high-tax nations, and codifying rules to make lower tax and poorer nations net losers. This proposal should be rejected.

7. "Digital Tax Erosion" is Not Occurring Due to Unfairness

The Blueprint's Pillar One is inconsistent with the widespread desire among nations to encourage the ubiquitous deployment of broadband services and associated applications. The idea of targeting the digital economy for additional taxation seem peculiar, considering that many nations provide direct subsidies and tax incentives within their countries to encourage the buildout and use of high-speed broadband internet services. Why tax the technologies that we should be encouraging?

Pillar One claims the need to fix the unfairness digital tax erosion problem, but empirical evidence of this unfairness is absent. Say, for example, a French company buys ad space from the U.S. social media company. Under the proposed tax plan, because the ads target French subscribers using the social media platform, possibly for free, a portion of the U.S. social media company's profits would be subject to taxation in France.

On the other hand, if the same French company were to buy ad space from the Financial Times newspaper, which is currently subscribed to readers all over the world, the Financial Times' earnings are not subject to taxation in France, but it would be if an end-user principle were evenly applied across all business sectors. Ironically, both social media platforms and newspapers, as well as any website, can publish its ads, but the tax implications are different by sector under the Blueprint. Clearly, from this example, the OECD Blueprint is not about "fairness"" and putting bricks and mortar purchases on the same footing with one another. The tax plan is designed to tax and competitively handicap only digital applications.[13]

The newspaper example is not an isolated one. The contradictory treatment of taxation between industries shows the absurdity of the assertion that the tax base is eroding. If there is a telephone order for a product to be shipped from Latvia to the U.S., if there is a mail catalog order from a Romanian company to Brazil, or if a German car producer ships its vehicles for sale in China, the Blueprint does not affect any of these cross-border transactions. However, if an Irish consumer simply hits "like" on a free social media platform, the social media company

[13] This example is from Steve Pociask, "OECD Tax Plan: Joe, Just Say No," *Morning Consult*, https://morningconsult.com/opinions/oecd-tax-plan-joe-just-say-no/.

could now subject to taxes, depending on its size. In summary, the proposed rules ignore parity and fairness between bricks and clicks businesses.[14]

8. Blueprint has a Bias Against Productivity Improvements That Will Harm Consumers

Tax policy should not impede global progress in operational efficiency and innovation. The digital economy has provided massive benefits, reduced costs, and lowered consumer prices. Through economies of scale and scope, per unit cost are decreased, and markets shift to improve operational efficiency. As they "do more with less," consumers benefit.

Technical change is needed to improve the welfare of society. For example, in 1950, there were 342,000 switchboard operators working in U.S. telephone companies plus another one million switchboard operators working elsewhere in the U.S. private sector.[15] Thanks to automation and computerization, as of May of 2019, the U.S. telecommunications sector employed only 790 operators.[16] This example shows the dynamic trend that has brought society nearly free Voice-over-Internet telephony services and free internet messaging services to consumers, governments and businesses. In 1950, had the U.S. used its tax code to protect operator service jobs, would society be better off today? Would social welfare have increased? How expensive would broadband services be today if every "click" on the computer's mouse required human intervention? How poor would consumers be without these technologies?

The Blueprint also seeks to apply a revenue test, exempting from taxation any multinational firm with total revenues below EUR 750 million. The figure is arbitrary. It also assumes incorrectly that different industries have similar economies of scale. Depending on the industry, taxing larger firms, while sparing other firms, could be a tax on efficiency.

The bottom line is that productivity fuels economic growth, creates new jobs, reduces the cost of living, improves the standard of living, and encourages future innovation. These technologies save time, money, and lives. Countries should embrace these changes and not erect protectionist barriers to prevent them.

9. The Blueprint Provides "Luddite" Anti-Technology Exemptions

As previously noted, the OECD Blueprint appears to focus on imposing additional taxes on high-tech companies, and this point is emphasized by a number of arbitrary exemptions regarding what should and should not be taxed. For instance, the Blueprint exempts an internet

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[14] Portions of these comments are taken directly from Steve Pociask, The OECD's Big Tech Cash Grab, *Real Clear Policy*, https://www.realclearpolicy.com/articles/2020/11/04/the_oecds_big_tech_cash_grab_582914.html, November 4, 2020.

[15] Telephone Switchboard Operators: Rise and Fall (bbntimes.com)

[16] "Occupational Employment and Wages: May 2019," U.S. Bureau of Labor Statistics, Table 43-2021 Telephone Operators, July 6, 2020, https://www.bls.gov/oes/current/oes432021.htm.

service provider that connects its customers across borders (using the Internet backbone) to reach social media sites, while a "free" social media service used by a consumer at one end of the connection is not exempt from taxation.[17] An online intermediary that books hotel rooms is taxed, but a similar service provided directly by the hotel is exempt. The Blueprint is slanted against the use of automation to achieve economies of scale where social media and search engines are taxed but customized online professional services are not. The added complexity of the Blueprint will produce a host of exclusions and carveouts that serve like protectionist tariffs and domestic trade barriers against competitive technologies and innovative services.

The inconsistencies described herein highlight the Luddite-like tax scheme setup to target high-tech companies and to benefit parts of the world's economies at the expense of U.S. tax coffers.[18] Moreover, how you define the digital economy could swallow up other major corporations that merely use e-commerce as another marketing channel to sell goods and services. Therefore, it should be of no surprise that the Pillar One initiative has little to do with tax erosion and is all about targeting large U.S. technology companies.

10. Taxes Act as Tariffs and Create Market Distortions

As far as Pillar One and Pillar Two, the U.S. has long been a global high-tech leader. Targeting U.S. firms or low-tax nations could eventually lead to retaliatory taxes or tariffs for the purpose of offsetting domestic losses.

Retaliatory measures aside, basic economics predicts that increased taxes on price sensitive goods and services will severely repress demand. Because digital applications and services are very often price elastic, taxing these services will be highly effective in reducing demand, but less effective in increasing government tax revenues. In other words, the value of the reduction in revenue could exceed the value of the tax collected. Unlike taxes on highly inelastic markets or on products associated with negative externalities, these taxes could be viewed as punitive and highly ineffective.

Among the possible responses to this include: the balkanization of high-tech businesses, as firms look to minimize their tax exposure across borders; and/or trade-like wars, as countries retaliate by imposing taxes or tariffs on cross border transactions. Online platforms would lose scale economies and network economies and reduce its cross-border functionality, which will reduce global innovation. Meanwhile, China could become the world's technology leader in developing online technologies – next generation wireless technology, artificial intelligence, online search, social media, facial recognition, and other technology applications. China could also then evade international tax payments by using its many shell corporations owned by the

[17] These examples come directly from Steve Pociask, The OECD's Big Tech Cash Grab, *Real Clear Policy*, https://www.realclearpolicy.com/articles/2020/11/04/the_oecds_big_tech_cash_grab_582914.html, November 4, 2020.

[18] Ibid.

communist government, and by cloaking its records in opaque financial reports. If this happens, what did the OECD accomplish and how exactly would this make society better off?

11. The Irony of Taxing Innovation

We have discussed here how technology is instrumental in spurring innovation and should not be singled out for taxation. In fact, during the COVID pandemic, online technologies have been instrumental in keeping the world's economy operating, providing telehealth applications, facilitating telecommuting, offering teleconferencing services, encouraging e-commerce to keep consumers socially distanced, and providing benefits to the environment. Noting the OECD tax project, one author recently commented:

> *It is doubly ironic that the project targets businesses providing online services, given that these businesses have been instrumental in keeping the global economy alive and governments functioning (not to mention education, social life, etc.) during the pandemic year of 2020. Good tax policy calls for heavier taxation of activities that cause harm to society, such as environmental degradation or direct harm to human health. Digital technology, however, in the words of the OECD itself, "spurs innovation, generates efficiencies, and improves services while boosting more inclusive and sustainable growth and enhancing well-being."*[19]

The Blueprint appears to be an attempt by some countries to expand its tax base beyond its borders at the expense of other countries. There is nothing fair about this tax scheme.

12. Concluding Remarks: The Need for a Comprehensive Reevaluation

As these examples have demonstrated, the proposed Pillar One and Pillar Two Blueprints will have dire consequences on some countries, industries, services, trade, and ultimately consumers. If a country wants to prevent tax erosion, its problem is with its own tax system.

To prevent tax erosion, countries should develop strategies and policies to compete, not collude as a tax cartel. If these tax plans become operational, countries will see their sovereignty eroded and taxing power ceded to international bodies. Unable to shop around, consumers and businesses will be the ultimate losers.

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[19] Jeff VanderWolk, "The OECD/Inclusive Framework's Digitalization Project: Politics Over Policymaking," Bloomberg, Bloomberg Tax – Daily Tax Report, December 8, 2020, [The OECD/Inclusive Framework's Digitalization Project: Politics Over Policymaking (bloombergtax.com)](bloombergtax.com).

As these comments have shown, the plan is riddled with inconsistencies that threaten double taxation and create implicit tariffs. By raising international taxes and limiting competition, this plan runs counter to the OECD's mission to "stimulate economic progress and world trade."[20] This Blueprint, if implemented, would have been a total failure, because it will have increased costs to businesses and consumers, repressed demand, harmed the environment, created artificial tax barriers, and reduced innovation. This point was reiterated by a tax expert writing for a major news organization:

> *Observers have noted the irony of OECD leadership of a project aimed at increasing taxes on cross-border trade and investment, given that the OECD was founded for the purpose of encouraging cross-border trade and investment … that doesn't sound like something we want to discourage through special taxes.*[21]

Because developing and finalizing these international tax rules has been an arduous process, it should be no surprise that, once agreed upon, these rules will become nearly permanent and even more difficult to modify in the future. Again, caution is strongly advised.

In conclusion, we recommend this plan be postponed at this time and its overarching framework be revised to be completely objective, nondiscriminatory, and consistent with universally accepted business and economic principles. At this time, the finetuning the minutia of the current Blueprint will not meet any of these fundamental and critical requirements.

Respectfully,

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[20] Holly Ellyatt, "Global Economic Hit from Coronavirus Will be Felt for a Long Time to Come," CNBC, March 23, 2020, https://www.cnbc.com/2020/03/23/coronavirus-oecd-warns-economic-hit-will-be-felt-for-a-long-time.html.
[21] Jeff VanderWolk, "The OECD/Inclusive Framework's Digitalization Project: Politics Over Policymaking," Bloomberg, Bloomberg Tax – Daily Tax Report, December 8, 2020, The OECD/Inclusive Framework's Digitalization Project: Politics Over Policymaking (bloombergtax.com).